United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

75-7359

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FOR THE SECOND CIRCUIT

No. 75-7359

THE HOME INSURANCE COMPANY,
Plaintiff-Appellee,

against

THE AETNA CASUALTY AND SURETY COMPANY
and DIAMOND SHAMROCK CORPORATION,
Defendants-Appellants.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF APPELLANT DIAMOND SHAMROCK CORPORATION

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Judgment Appealed From

The Judgment appealed from was signed by Hon Robert L. Carter, U.S.D.J., on May 9, 1975 and entered on May 13, 1975 (135a-136a).* Judge Carter's opinion (120a-134a) is reported in Ins. L. Rep. (Fire & Casualty Cas.) at 75-792.

Statement of Issues Presented for Review

(1) Was appellant Diamond Shamrock Corporation ("Diamond") entitled to a declaratory judgment that there

* References are to pages in the Appendix.

had been two occurrences for purposes of Diamond's insurance policies from The Aetna Casualty and Surety Company ("Aetna") and The Home Insurance Company ("Home") or, as the District Court held, was Home entitled to a declaratory judgment that there had been four occurrences?

(2) Did the District Court err by failing to resolve in Diamond's favor ambiguities in the insurance policies of Home and Aetna with respect to the number of occurrences?

(3) Did the uncontroverted evidence as to pertinent custom and usage within the insurance industry require the District Court to find that there had been two occurrences for purposes of Diamond's policies from Aetna and Home?

(4) Did the affidavits submitted by Diamond, Aetna, and Home create genuine issues of fact which should have precluded the District Court from granting Home's motion for summary judgment?

Statement of the Case

A. Nature of the Case, Course of Proceedings and Disposition.

The present case is an action for declaratory judgment pursuant to 28 U.S.C. §§ 2201-2202 and was commenced by Home against Diamond and Aetna on September 24, 1974. Home's complaint (5a-9a) sought a determination that, for purposes of Diamond's primary insurance policy with Aetna and Diamond's excess policy with Home, there had been four "occurrences" with respect to damage caused by defective goods which Diamond produced.

Home moved for summary judgment by notice of motion dated October 28, 1974 (10a-23a). Diamond answered the complaint (40a-43a) and cross moved for summary judgment on November 5, 1974 (24a-43a); Aetna answered (44a-

45a) and also cross moved for summary judgment on November 13, 1974 (46a-52a).

With its motion papers, Home submitted the affidavit of its Excess Claims Division Supervisor, Robert H. Burns, sworn and subscribed to October 21, 1974 ("Burns Affidavit"; 12a-18a).

Diamond submitted with its motion papers affidavits of the following persons: (i) Charles M. Ely, Manager of Agricultral Research and Technical Services for Diamond's Nutrition and Animal Health Division, sworn and subscribed to October 31, 1974 ("Ely Affidavit"; 28a-29a); (ii) F. Gordon Steward, Production Manager for Nutrition and Animal Health Products at Diamond's Harrison, New Jersey plant, sworn and subscribed to October 31, 1973 ("Steward Affidavit"; 30a-31a); (iii) Marvin T. Grieder, Products Manager of Feed Supplements in Diamond's Nutrition and Animal Health Division, sworn and subscribed to October 31, 1974 ("Grieder Affidavit"; 32a-33a); (iv) William R. Greening, Vice President of Alexander & Alexander, Inc., sworn and subscribed to November 5, 1974 ("Greening Affidavit"; 34a-35a); and (v) Michael Collins, Assistant Vice President of Alexander & Alexander, Inc., sworn and subscribed to November 4, 1974 ("Collins Affidavit"; 37a-39a).

Aetna submitted with its motion papers the affidavit of Otto Kaufmann, Jr., Aetna's manager of the New York National Accounts Office, sworn and subscribed to November 13, 1974 ("Kaufmann Affidavit"; 50a-52a).

Home served answering papers (53a-119a) on November 21, 1974, which contained the affidavit of Arthur J. Mella, Home's Excess Claims Manager, sworn and subscribed to November 20, 1974 ("Mella Affidavit"; 55a-62a). Diamond and Aetna submitted a joint reply memorandum dated December 12, 1974.

On April 24, 1974, the District Court issued an opinion (the "Opinion") (120a-134a) granting Home's motion for summary judgment and denying defendants' separate cross motions. This opinion was embodied in a final judgment, which was signed by Judge Carter on May 9, 1975 and entered on May 13, 1975 (135a-136a).

B. Statement of Relevant Facts.

The present case stems from Home's attempt to evade the full extent of its liability to Diamond under an excess insurance policy.*

The events which give rise to the controversy between Diamond and Home are not in dispute. Diamond produces superconcentrated Vitamin D3 resin in its plant at Harrison, New Jersey ("Ely Affidavit" at ¶3; 28a-29a). The resin is melted to form a blend and Diamond sometimes sells the resin in that form to customers ("Ely Affidavit" at ¶3; 28a-29a). After melting to form a blend, the resin is sometimes mixed in corn oil and sold to customers in that form ("Ely Affidavit" at ¶3; 28a-29a). Or, finally, the resin after melting and mixing with corn oil is sometimes shipped to Diamond's vitamin premix plants at Louisville, Kentucky, Van Buren, Arkansas, and Fresno, California, for the production of dry Vitamin D3 concentrates ("Ely Affidavit" at ¶3; 28a-29a).

In the course of manufacturing operations at Diamond's Harrison, New Jersey plant, two lots of superconcentrated Vitamin D3 resin were produced and denominated as lots C498 and C500 ("Steward Affidavit" at ¶2; 30a-31a). These two lots of blended superconcentrated Vitamin D3 resin were subsequently mixed with corn oil and antioxidants at Harrison and then shipped to Diamond's plant in Louisville ("Steward Affidavit" at ¶2; 30a-31a).

* Home's policy with Diamond is # HEC 4165987 (the "Home Excess Policy") ("Burns Affidavit" at ¶2; 12a-13a).

An investigation conducted by Diamond personnel determined later that both lot C498 and lot C500 had been rendered inactive as a result of accidents which occurred during melting and blending at the Harrison plant—prior to shipment to Diamond's plant in Louisville ("Ely Affidavit" at ¶6, 29a; "Steward Affidavit" at ¶3, 31a).

At Diamond's Louisville plant, lots C498 and C500 were sprayed onto corn cob fractions to make four lots of Nopdex "200" (Home's Statement pursuant to General Rule 9(g) at ¶4(c), 22a); Diamond's Statement pursuant to General Rule 9(g) at ¶1, 25a-26a). The four Louisville lots were thus defective because the Harrison lots C498 and C500 had been defective (Opinion at 3; 123a).*

Diamond sold the four Louisville lots to Central Soya Corporation ("Central Soya") which used them in making chicken feed. Central Soya in turn sold its chicken feed product to numerous chicken farmers who ultimately suffered property damage because their poultry's ingestion of the defective chicken feed resulted in "various afflictions, including rickets, abnormal growth, defective egg production and death" (Opinion at 3; 123a).

Central Soya has been engaged in settling claims made by the damaged chicken farmers and Diamond concedes its liability to Central Soya in the amount of these claims (Opinion at 3; 123a).

At all times relevant, Diamond was insured with respect to property damage caused by its goods or products under a comprehensive liability policy issued by Aetna (the

* Though averring no facts which would indicate personal knowledge of the operations of Diamond's Louisville plant, the Burns Affidavit at ¶5(c) states that Diamond "further processed" lots C498 and C500 in Louisville by "grinding" and by "blending with oil" (14a). The Grieder Affidavit at ¶3 (33a), offered by Diamond and made on personal knowledge, however, unequivocally states that no grinding or blending with oil occurs at the Louisville plant. Moreover, *Home's Answering Statement Pursuant to General Rule 9(g) concedes that lots C498 and C500 became defective because of a production mistake at Diamond's Harrison plant* (53a).

"Aetna Underlying Policy") and under the Home Excess Policy. The Aetna Underlying Policy (110a-119a) insured Diamond against liability for property damage up to $250,000 per occurrence, subject to a deductible of $100,000 per occurrence (Home's Statement Pursuant to General Rule 9(g) at ¶¶1-2, 19a-20a; Diamond's Statement Pursuant to General Rule 9(g) at ¶1, 25a-26a).

Under the Aetna Underlying Policy, the "named insured's products" were defined as:

> goods or products manufactured, sold, handled or distributed by the named insured or by others trading under his name, including any container thereof (other than a vehicle), but named insured's products shall not include a vending machine or any property other than such container, rented to or located for use of others but not sold.

Under the definitions in the Aetna Underlying Policy,

> "occurrence" means an accident including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured.

Additionally, the Aetna Underlying Policy contains a "batch clause", which states in relevant part:

> . . . AS RESPECTS PRODUCTS LIABILITY FOR BODILY INJURY AND PROPERTY DAMAGE COVERAGE:
>
> ALL SUCH DAMAGE ARISING OUT OF ONE LOT OF GOODS OR PRODUCTS PREPARED OR ACQUIRED BY THE NAMED INSURED OR BY ANOTHER TRADING UNDER HIS NAME SHALL BE CONSIDERED AS ARISING OUT OF ONE OCCURRENCE.

(Diamond's Statement pursuant to General Rule 9(g) at ¶1, 25a- 26a; Joint Submission, 117a.)

The Home Excess Policy indemnified Diamond up to $3,000,000 per occurrence for liability arising out of prop-

erty damage in excess of the Aetna Underlying Policy's coverage, subject to the same definitions as in the underlying policy ("Burns Affidavit" at ¶¶3-4, 13a; Diamond's Statement pursuant to General Rule 9(g) at ¶1, 25a-26a).

Based upon its intent and understanding with respect to the meaning of occurrence as clarified by the "batch clause", Diamond has taken the position that there were two occurrences for purposes of its policies with Aetna and Home, i.e., one occurrence for each of the two defective lots produced at the Harrison plant from which property damage arose (Diamond's Statement Pursuant to General Rule 9(g) at ¶¶5-6; 26a-27a). Home, on the other hand, contends that there were four occurrences, one for each of the four defective Louisville lots sold to Central Soya. (Home's Statement pursuant to General Rule 9(g) at ¶6; 23a).

Both Diamond and Aetna offered evidence in the Greening Affidavit (34a-36a) and the Kaufmann Affidavit (50a-52a) with respect to the intended meaning of "occurrence", as well as insurance industry custom and usage pertaining to that term as clarified by the batch clause. Briefly summarized, this evidence indicated that Aetna had provided general liability coverage for Diamond for at least the last 15 years ("Kaufmann Affidavit" at ¶2; 50a). During that time, the Aetna policies contained a batch clause identical to the one in the present Aetna Underlying Policy ("Greening Affidavit" at ¶5, 35a-36a; Kaufmann Affidavit at ¶2, 50a).

In November 1966 the National Bureau of Casualty Underwriters adopted for insurance industry use a revised general liability policy which eliminated the batch clause and defined "occurrence" as it appears in the present Aetna Underlying Policy; this was done because the National Bureau believed that the new definition of occurrence had the same effect as the batch clause ("Greening Affidavit" at ¶¶2-3, 34a-35a; "Kaufmann Affidavit" at ¶¶3-4, 50a-51a).

Diamond's general liability policy had been negotiated with Aetna in February 1966 for a three-year term and, around the renewal date of February 1, 1969, Alexander & Alexander, as the insured's broker, approached several insurers to find one which would retain the batch clause ("Greening Affidavit" at ¶4; 35a). The Greening Affidavit at ¶5 (35a-36a) states that Alexander & Alexander's purpose in seeking a continuation of the batch clause

> ... was to clarify the intent to limit the amount of loss incurred by the insured, consistent with the concept of an occurrence, since Diamond Shamrock was on a cost plus basis providing for reimbursement to the carrier by the insured up to a certain limit of loss in the primary casualty contract. Aetna and Alexander & Alexander agreed to renewal of the policy in February 1969 with inclusion of the "batch" clause, so that there would be one occurrence for each batch or lot with respect to which an accident occurred.

The Kaufmann Affidavit at ¶6 (51a) confirms this and states at ¶7 (51a) that Diamond

> insisted on this batch clause in order to minimize its losses under the policy because it was on a retrospective rating plan and it was to its financial interest to keep to a minimum consistent with the concept of [an] occurrence under the policy the number and amount of losses. This was understood by both parties to the insurance contract.

As to insurance industry custom and usage with respect to the batch clause, the Collins Affidavit at ¶4 (38a) indicates that once a batch or lot acquires a separate integrity and an administrative number for accounting and production purposes, a lot within the meaning of the batch clause comes into existence. Thus, the number of occurrences derives from the number of identifiable lots which are first produced and to which an accident occurs or has occurred.

Home also offered evidence on insurance industry custom and usage in the Mella Affidavit (55a-62a). This affidavit states that the only "industry-wide understandings" concerning the interpretation of insurance policies are that:

> . . . the final arbiter of the meaning of an insurance policy is a Court called upon to interpet it, and . . . Courts will interpret policies based upon the common or popular meaning of the words used therein (56a).

The Mella Affidavit also purports to contradict the Greening and Kaufmann Affidavits with respect to the intention of the National Bureau of Casualty Underwriters in its 1966 revision of the definition of occurrence. Yet Home's affiant offers only two irrelevant documents: an October 6, 1964 memorandum (63a-71a) and an address (72a-85a) by one R. J. Wendorff at a 1966 section meeting of the American Bar Association, whose references to the definitional changes made in "occurrence" pertain only to the recurrent issue of whether an "occurrence" took place within the time period of a policy's coverage, rather than the issue here of how many occurrences there were.

The Mella Affidavit at ¶13 (60a-61a) attempts to controvert the Collins Affidavit as to insurance industry custom and usage concerning the batch clause. Home's affiant, however, merely states that he is unaware of any such custom or usage as described in the Collins Affidavit (60a).

ARGUMENT

The plain meaning of both "occurrence" and the batch clause required the District Court to hold that there had been two occurrences for purposes of Diamond's policies from Home and Aetna. The District Court should have applied the rule of *contra proferentem* to resolve any ambiguity as to the number of occurrences in favor of Diamond,

the insured, and against Home. The uncontroverted evidence as to insurance industry custom and usage with respect to the batch clause clearly mandated a determination that there had been two occurrences under Diamond's policies with Home and Aetna. Alternatively, the District Court failed to recognize that there existed genuine issues of fact about insurance industry custom and usage as to the batch clause and should have denied all parties' motions for summary judgment.

A. The District Court erred in applying the policy definition of occurrence

At all times relevant, the Aetna Underlying Policy defined "occurrence" as

> an accident . . . which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured.

This definition the Home Excess Policy adopted by reference. As can be readily apprehended from the words themselves, an "occurrence" requires the presence of two factors: there must be (1) an accident and (2) the accident must result in bodily injury or property damage, neither expected nor intended from the standpoint of the insured. In this case, there were two accidents, namely the two production mistakes at Diamond's Harrison, New Jersey plant which yielded the two defective lots of Vitamin D3 resin. These two accidents in the production of Vitamin D3 resin each resulted in damage to the property of poultry farmers. Since there were two accidents, each of which resulted in property damage, there were thus two occurrences for purposes of Diamond's policies from Home and Aetna.

The District Court, however, departed from the plain meaning of "occurrence" to hold that there had been an

occurrence each time one farmer fed chicken feed containing the defective Vitamin D3 resin to his chickens at a single time and place (Opinion at 10; 130a).*

This erroneous conclusion was based upon the District Court's misapplication of *Arthur A. Johnson Corp.* v. *Indemnity Co.*, 7 N.Y.2d 222, 164 N.E.2d 704, 196 N.Y.S.2d 678 (1959) and *Hartford Accident & Indemnity Co.* v. *Wesolowski*, 33 N.Y.2d 169, 305 N.E.2d 907, 350 N.Y.S.2d 895 (1973).** Neither of these cases is directly relevant to the interpretation of "occurrence" in Diamond's policies with Home and Aetna since neither case involved a definition of that term corresponding to the one presented here. The *Johnson* case involved an insurance policy covering "injury . . . caused by accident," where "accident" was not defined. The *Wesolowski* case involved an automobile liability policy with a limitation on liability "per occurrence" but the facts, as stated by both the Appellate Division and the New York Court of Appeals, nowhere disclose that "occurrence" was defined as in the Aetna Underlying Policy. Moreover, both parties to that case urged that the

* The District Court's analysis, of course, rested solely upon the Aetna Underlying Policy's definition of occurrence and did not take into account the batch clause. The District Court's stress on *immediacy* in discussing the "accidents" reveals its apparent misunderstanding of the record as to how the Harrison lots were defective. Nothing contained in the record supports the idea, as stated by the District Court, that the lots contained "poison" or that chickens were "poisoned" or that "ingestion of poison" resulted from a single feeding (Opinion at 9, 10; 129a-130a). The uncontroverted evidence, instead, is that the two Harrison lots of superconcentrated Vitamin D3 became inactive before leaving Diamond's Harrison plant ("Steward Affidavit", ¶¶2-3; 30a-31a). Thus, chickens fed the ultimate chicken feed containing the defective (i.e., inactive) Vitamin D3 failed to receive or ingest the intended nutritive supplement and, in turn, were susceptible to and developed various afflictions or diseases (Complaint at ¶8(f), 7a; Diamond's Answer at ¶4, 41a).

** Diamond does not contest the District Court's conclusion that New York law should govern this action where subject matter jurisdiction is based upon diversity.

words "accident" and "occurrence" were synonymous, a view which the New York Court of Appeals accepted only in the context of that case.*

The District Court here, however, reasoned that, under *Wesolowski* and *Johnson*, occurrence as defined in the Aetna Underlying Policy must mean "accident" and that "accident" must mean an event "which *immediately* preceded or occurred simultaneously with the damage" (Opinion at 9; 129a). Not only does this obviously apply *Johnson* and *Wesolowski* beyond their express limits, it also flies directly in the face of the Aetna Underlying Policy's definition of "occurrence." Again, that definition does not equate "occurrence" with "accident" but states that occurrence is an accident which results in damage. Furthermore, this definition imposes no requirement that the accident must take place immediately prior to or simultaneously with damage.** If "accident" and "occurrence" are simply congruent for purposes of the Aetna Underlying Policy, then that portion of the definition requiring the accident to result in damage is superfluous and its insertion serves no purpose. New York law, however frowns upon a construction which would render any portion of a contract superfluous. See 6 L. Simpson and R. Duesenberg, *Encyclopedia*

* "Past cases have used the words interchangeably and we agree that no distinction should be drawn on this basis in the present case." 33 N.Y.2d at 172-173, 305 N.E.2d at 910, 350 N.Y.S.2d at 899. Indeed, the Court even reiterated this limitation: "We repeat, however, we see no occasion to find any difference between the two nouns for present purposes." 33 N.Y.S.2d at 173, n.1., 305 N.E.2d at 910, n.1., 350 N.Y.S.2d at 899, n.1.

** This reasoning further exposes the District Court's confusion. The Court starts with two premises: (1) occurrence=accident and (2) the accident must take place immediately prior to or simultaneously with damage. An obvious corollary to the second premise is that accident is different from damage. Under the first premise, however, occurrence=accident and, therefore, occurrence must be different from damage. Yet the Aetna Underlying Policy defines occurrence so as to include damage. Thus, the first premise which yields this contradictory result must be incorrect.

of New York Law: Contracts § 813 at 484-485 nn.11-12 (1963).*

While the Aetna Underlying Policy contains no definition of "accident", the District Court falls into the error of assuming that this term has some fixed judicial meaning which must apply to every manifestation of this word in an insurance policy. As the New York Court of Appeals, stated in *Croshier* v. *Levitt*, 5 N.Y.2d 259, 262, 157 N.E.2d 486, 487, 184 N.Y.S.2d 321,323 (1959), however:

> No all-inclusive definition of 'accident' is possible, nor any formulation of a test applicable in every case, for the word has been employed in a number of senses and given varying meanings depending upon the relevant context.

Accord, *McGroarty* v. *Great American Insurance Company*, 36 N.Y.2d 358, 329 N.E.2d 172, 368 N.Y.S.2d 485 (1975); 30 N.Y. Jur., *Insurance* § 1099 (1963).**

The relevant context here is that Diamond, a major chemical company, must necessarily obtain comprehensive liability insurance to protect itself against damage claims arising out of its products which are possibly defective, as here where defective goods prepared at the Harrison plant

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* *See also Restatement (Second) of Contracts*, Explanatory Notes § 229, comment *b* at 516 (Tent. Draft Nos. 1-7, 1973): "Since an agreement is interpreted as a whole, it is assumed in the first instance that no part of it is superfluous." Though this comment goes on to note that even "tailor made" agreements may contain superfluous or redundant terms, the District Court offers no reason why the second element in the Aetna Underlying Policy's definition of occurrence should be considered superfluous or redundant.

** The District Court ought to have heeded the warning of Mr. Justice Holmes against mechanically applying a prior construction of some word or phrase without regard to the context in which the expression is used: "A word is not a crystal, transparent and unchanged, it is the skin of a living thought and may vary greatly in color and content according to the circumstances and the time in which it is used." *Towne* v. *Eisner*, 245 U.S. 418, 425 (1918).

gave rise to just such claims.* Thus, Diamond has obtained insurance coverage for products liability such as that occasioned by the accidents at the Harrison plant.

To construe "accident" in the Aetna Underlying Policy as referring to a production mistake such as that which occurred at the Harrison plant is fully supported by the basic rule that an insurance policy must be construed with respect to the risk insured. *See* 1 Couch *Insurance* 2d § 15:26 (1959).

Authority from other jurisdictions confirms that "accident," as used in the Aetna Underlying Policy, should refer to the two production mistakes at the Harrison plant.**

Thus, *Andrews & George Co. Ltd.* v. *Canadian Indemnity Co.*, [1952] 1 D.L.R. 180 (Brit. Col. Ct. App. 1951) *rev'd on other grounds* [1952] 4 D.L.R. 180 (Canad. Sup. Ct. 1952), held that a defect in manufacture constituted an "accident" under the plaintiff's insurance policy from the defendant. In this case the plaintiff, a manufacturer of glue, had obtained insurance with respect to "liability imposed by law" for "damage caused by accident." Certain glue manufactured by Andrews & George Co. Ltd. was sold to a lumber company which used it in the manufacture of plywood. Subsequently, it was discovered plaintiff's glue had been defective, rendering the plywood below standard. The plaintiff paid the lumber company its loss from the sub-

* To argue that Diamond obtained insurance against the risk from possible harm occasioned by its goods *passing* to third parties simply misses the point. In the ordinary course of business, Diamond's goods do pass to third parties; no risk is involved there. But in the ordinary course production mistakes, such as the accident at the Harrison plant, which created defective goods, do not happen; and it is this risk against which Diamond has obtained insurance.

** While appellant has referred to New York authority in construing "accident," there appear to be no New York cases directly on point as to whether "accident" would encompass a production error, such as occurred at the Harrison plant. As discussed, *infra*, there also appears to be no direct authority, whether from New York or any other jurisdiction, which construes a batch clause.

standard plywood but defendant's insurance company denied any liability. The Court of Appeals correctly reasoned that it was clear that "accident" had to refer to an accident in the manufacture of the glue:

> Damage could only happen if there was a fault in the manufacture of the glue. Unless the accident applies to something in the manufacture of the glue and damage to property of a purchaser resulting from such accident, the appellant got no advantage from the insurance. I think therefore that the word "accident" applies to some defect arising in the manufacture of the glue.* [1952] 1 D.L.R. at 183-184.

Ramco, Inc. v. *Pacific Insurance Company*, 249 Or. 666, 673, 439 P.2d 1002, 1005 (1968) accepts the reasoning of the British Columbia Court of Appeals that

> . . .the meaning of the word "accident" must be relevant to the kind of product being manufactured by insured and to the kind of loss that it could sustain by reason of a defect in manufacture.

In that case a manufacturer of heaters covered by an insurance policy for "loss caused by accident" recovered against its insurance carrier which had denied liability when the insured's defective heaters caused damage to a motel in which they had been installed.** *See also, Koehring Co.* v.

* In reversing, the Canadian Supreme Court held that the insured's payment of damages to the lumber company had not been a "liability imposed by law." Two Justices agreed with the Court of Appeals' conclusion on accident; two dissented from this conclusion; and one expressed no opinion on that issue.

** The relevance of this case to the *reasoning* necessary for a proper construction of "accident" is not diminished by the fact that the policy in question defines "products hazard," for which insurance coverage was issued, to require the "accident" to take place *after* the insured has relinquished possession of the products. Significantly, "products hazard", as defined in the Aetna Underlying Policy says only that damage must occur after the insured has relinquished its products—which bolsters appellant's contention that "accident" refers to the production mistake at Diamond's Harrison plant.

American Auto Insurance Co., 353 F.2d 993 (7th Cir. 1965); *Beacon Textiles Corporation* v. *Employer's Mutual Liability Insurance Company*, 355 Mass. 620, 246 N.E.2d 671 (1969). Thus, 2 R. Hursh, *American Law of Products Liability* § 10:5 (1961) states at 93-94:

> It has also been held that an "accident" covered by insurance against liability for loss "caused by accident" comprehends a loss traceable to a product which, because of some unexplainable, unexpected, and chance error in the insured's manufacturing process is defective.

Finally, a careful analysis of the rationale underlying the New York Court of Appeals' decisions in *Johnson* and *Wesolowski* indicates that these two cases support the view that "accident" in the Aetna Underlying Policy refers to the production mistakes at the Harrison plant. In *Johnson**, an insured contractor, in the course of doing excavation work for subways, removed the underground vault walls in front of two buildings which had adjoining, but separate, sub-basements. In place of these removed walls, the contractor built two separate, temporary walls enclosing the fronts of the two sub-basements. Sometime thereafter, a "rainfall of unprecedented intensity" flooded the excavation. One of the temporary walls gave way and its sub-basement flooded. Fifty minutes later the other sub-basement was flooded by the collapse of its temporary wall.

Faced with the question of how many accidents there had been for purposes of determining the extent of the insurance carrier's liability, the New York Court of Appeals reviewed the approaches to defining "accident" which had emerged from other jurisdictions. One line of authorities

* As discussed, *supra*, this case involved a policy covering damages caused by "accident."

held that where one factor is the sole proximate cause, there is only one "accident" though there may be several resultant injuries. The other approach held that for each person who has suffered a loss there has been an accident. The Court of Appeals, however, chose as the soundest approach for the case before it the view that an accident constitutes an unexpected and unfortunate event. In supporting this conclusion the Court stated:

> This approach of determining simply whether there was one unfortunate event or occurrence seems to us to be the most practical of the three methods of construction which have been advanced because it corresponds most with what the average person anticipates when he buys insurance and reads the "accident" limitation in the policy. 7 N.Y.2d at 229, 164 N.E.2d at 708, 196 N.Y.S.2d at 684.

From this approach, the Court reasoned that there had been two accidents, namely the collapse of the two temporary walls, because the two walls had collapsed at different times and the collapse of one had not caused the collapse of the other.

First, applying this rationale to the present case clearly supports the contention that there were two accidents and hence two occurrences. The accidents which rendered the two lots inactive and defective certainly constituted unexpected and unfortunate events. Moreover, the accident to the first lot was distinguishable in time and space from the accident to the other. Furthermore, the contamination of the first lot did not cause the contamination of the other.*

* The *Johnson* rationale provides no support for the contention that there were four accidents and hence four occurrences. Contamination, the unfortunate and unexpected occurrence, had already taken place before four lots emerged from the two. Thus, no logical argument can be made that the four lots became contaminated in separate and unrelated events. Spreading rancid butter on different slices of bread does not yield four instances where butter became rancid.

Second, the District Court apparently misunderstood the *ratio decidendi* of the *Johnson* case, which simply does not support the District Court's conclusion that the New York Court of Appeals:

> rejected the view that the policy term "accident" referred to an act by the insured, and that the number of "accidents" was dependent on the number of acts by the insured which proximately caused the damages. (Opinion at 6; 126a)*

Yet the *Johnson* court did not hold that an unfortunate and unexpected act could not be an act of the insured. The view which the New York Court of Appeals did reject—and the only one advanced by the defendant insurance company—was that the rainfall was *the* proximate cause of all damage, a contention the court found factually untenable.** Furthermore, the *Johnson* court itself strongly suggested that its "event test" was not incompatible with resort to the cause of damage for determining the number of accidents, when the latter test was properly applied:

> In the instant case, it cannot be said that one would allege but one act of negligence as the proximate cause of the injuries to the two separate properties. Here the proximate cause cannot be said to be the heavy rainfall but separate negligent acts of preparing and constructing separate walls which, for all we know, may have been built at separate times by

* The District Court appears to reiterate this view of *Johnson*, though in somewhat cryptic fashion, by stating that the New York Court of Appeals:

> . . . rejected the view that the number of accidents is equivalent to the number of acts by the defendant [*sic*] which proximately caused the injuries. (Opinion at 7; 127a).

The District Court must mean "insured" rather than "defendant," since in the *Johnson* case, the insurance company was the defendant.

** In addition, the catastrophe was not the rain—that, in itself, did no harm." 7 N.Y.2d at 230, 164 N.E.2d at 708 196 N.Y.S.2d at 684.

> separate groups of workmen. 7 N.Y.2d at 230, 164 N.E.2d at 708, 196 N.Y.S.2d at 684*

Finally, *Allied Grand Doll Manufacturing Co.* v. *Globe Indemnity Co.*, 15 App. Div. 2d 901, 225 N.Y.S.2d 595 (1962), which held that damage caused by a water faucet left on over a weekend constituted one accident under the applicable insurance policy, reads the *Johnson* "event test" as permitting reference to an act by the insured:

> In [*Johnson*], it was not the rainstorm and flood which created the liability or determined the scope of the coverage; *it was the several and separate acts done by the plaintiff* in an attempted fulfillment of certain duties which were inadequately done. As there pointed out, these distinct duties which were attempted to be met by separate acts created severable liabilities. Therefore, when the walls of the different buildings collapsed, it was held there was more than one accident. 15 App. Div. 2d at 901, 225 N.Y.S.2d at 596.** (emphasis added)

The District Court's reliance upon *Wesolowski* similarly involves a misapprehension of the reasoning in that case. There the New York Court of Appeals held that one car's sideswiping of a second car, immediately followed by the first car's head-on collision with a third constituted one "occurrence" for purposes of the insurance policy in issue.*** While applying the event test, the New York Court

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* Since the Court's reason for applying an "event" test was the expectation of the insured, it would seem more reasonable in the present case, where the insured is a manufacturer, to recognize that the unfortunate event was the defect at the Harrison plant which was the cause of injury to the chickens.

** Thus a Federal District Court in a diversity action has interpreted and applied a decision by the New York Court of Appeals in a manner diametrically opposed to that of the second highest court of the State.

*** As discussed *supra*, both parties in *Wesolowski* agreed that "occurrence" meant the same thing as "accident."

of Appeals again predicated that choice upon the expectation of the insured.* The court also offered a digression on the possible difference between "occurrence" and "accident":

> To the extent that there is any distinction between the two words, "occurrence" would appear more closely to approximate "event". It is defined as "1. An act or instance of occurring. 2. Something that takes place; an incident" (The American Heritage Dictionary of the English Language, 1969, p. 908). On the other hand, an "accident" is defined as "1. An unexpected and undesirable event; a mishap. 2. Anything that occurs unexpectedly or unintentionally", *op. cit.*, p. 8. Thus, the latter definition suggests a connotation as to causation, while the former is more objectively descriptive of what occurred rather than being in any way related to how or why. We repeat, however, we see no occasion to find any difference between the two nouns for present purposes. 33 N.Y.2d at 173, n.1, 305 N.E.2d at 910, n.1, **350 N.Y.S.2d at 899, n.1.**

This observation clearly indicates that with respect to "occurrence", as defined in the Aetna Underlying Policy,** "accident" should be read as connoting the cause of damage, namely the production mistakes at Harrison, while

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*"We see no reason why we should now adopt a different standard or test merely because the question in the case before us arises under an automobile liability policy rather than a contractor's public liability policy. On the contrary, the perspective and expectation of the ordinary purchaser of either type of insurance would be the same." 33 N.Y.2d at 173 305 N.E.2d at 910, 350 N.Y.S.2d at 899. Different expectations, however, exist with respect to the purchaser of the insurance for products liability, which *Ramco, Inc.* v. *Pacific Insurance Company*, 249 Or. 666, 670, 439 P.2d 1002, 1003-4 (Or. Sup. Ct. 1968) recognizes:

> ". . . products liability coverage is obtained and premiums paid for purposes differing from the more common form of public liability insurance."

** "an accident . . . which results in damage."

"occurrence" encompasses both the accident and the resulting damage caused by the accident. Inexplicably, the District Court stands the observation of the New York Court of Appeals in *Wesolowski* upon its head:

> According to [the New York Court of Appeals' view], retention of the term "accident" in the [Aetna Underlying Policy] after 1966 might have given some support to defendants' position that events at the Harrison plant constituting the proximate cause of the damage were the "accidents." (Opinion at 9, n.4; 129a.)

Yet the Aetna Underlying Policy did *retain* "accident" as that term was used in the definition of "occurrence".

Finally, neither *Johnson* nor *Wesolowski*, when correctly analyzed, provides any support for the District Court's reasoning that "accident" should refer to the farmers' feeding their poultry chicken-feed rendered defective by the production mistakes at the Harrison plant. Feeding chickens is an event which is hardly unforeseen and, far from being unexpected, is in fact anxiously awaited by the chickens and clearly intended by the farmer. While it was unfortunate that chickens were fed defective chicken-feed, the unfortunate events in this sequence were the production mistakes at the Harrison plant, which gave rise to the chain of causation resulting in the chickens' ingestion of defective food.

B. The District Court erred in holding that the batch clause did not limit the number of occurrences to two.

Even if the Aetna Underlying Policy's definition of occurrence may leave some doubt as to the number of occurrences in this case*, the plain meaning of the batch

* The Home Excess Policy, of course, adopts the batch clause as well as the definition of occurrence. *See* Burns Affidavit at ¶4; 13a-14a.

clause clearly indicates that there were only two occurrences. That clause provides, in pertinent part, that all

> . . . damage arising out of one lot of goods or products prepared or acquired by the named insured or by another trading under his name shall be considered as arising out of one occurrence.

In applying this clause, the District Court erroneously concluded that the term "goods or products" could only refer to the goods which Diamond sells to third parties. The only reason given for this result is the general rule of construction that an insurance policy must be construed according to the understanding of the average businessman who purchases the policy and the District Court's view that this construction follows "common sense". While Diamond does not quarrel with the cited* rule of construction, its application to the present case does not support the District Court's result. First, this result simply overlooks the definition of the named insured's products contained in the Aetna Underlying Policy, which includes "goods or products manufactured, sold, handled or distributed" by Diamond. This definition certainly does not require that goods or products must be sold to be covered by the policy. Such a requirement would be sound only if the word "and" were inserted in place of the disjunctive term "or" in the sequence "manufactured, sold, handled or distributed."

* Neither case adduced by the District Court to sustain this rule bears directly upon the definition of "goods and products." *Tyroler v. Continental Casualty Co.*, 31 App. Div. 2d 8, 294 N.Y.S.2d 373 (1968), *aff'd*, 25 N.Y.2d 710, 255 N.E. 2d 560, 307 N.Y.S.2d 219 (1969), deals with the construction of the meaning of hospital care in a medical policy. While the other case, *Thomas J. Lipton, Inc. v. Liberty Mutual Insurance Co.*, 34 N.Y.2d 356, 314 N.E.2d 37, 357 N.Y.S.2d 705 (1974) does involve an insurance policy covering products liability, the issue presented there was whether the policy excluded damage arising out of a third party's removal from the market of the insured's products or products into which they had been incorporated.

Moreover, the District Court's construction contravenes the definition given "goods" and "products" in the dictionary. Thus, *Webster's Third International Dictionary* at 978 (1961) defines "goods" in relevant part (No. 3b): "chattels, wares, merchandise, food products, *chemical compounds* . . ." (emphasis supplied) and at 1810 defines "products" in pertinent parts: "something produced by physical labor . . ." (No. 2a) and "a substance produced from one or more other substances as a result of chemical change." (No. 4). In short, once a substance has been manufactured, it constitutes a good or product for purposes of the batch clause. Surely, the common sense of an ordinary businessman would tell him that the two Harrison lots which his plant had manufactured were in fact his goods or products and therefore within the purview of the batch clause, particularly after reading the policy's definition. Furthermore, superconcentrated Vitamin D3 resin, after melting and blending at Harrison, is sometimes sold by Diamond to customers; and the same product actually shipped to Louisville from Harrison is sometimes instead sold by Diamond directly to third parties. Thus, the two Harrison lots consisted of a substance which clearly constitutes a good or product of Diamond for purposes of the batch clause.* Finally, the District Court's reasoning that the Harrison lots were not "goods or products" rests upon its contrivance that these lots were "ingredients" (Opinion at

*In a tone reminiscent of Humpty-Dumpty's boast to Alice that words meant only what he said they did, the District Court held the above fact irrelevant to its construction of "goods or products":

> That fact is not significant since the defective resin here was clearly an ingredient which did not meet the definition of "goods or products," *as I have construed it here* (emphasis supplied). (Opinion at 12, n.7; 132a.)

Compare, C. Dodgson ("L. Carroll") *Alice's Adventures in Wonderland* and *Through the Looking Glass* at 186 (New Amer. Lib. 1960): " 'When I use a word,' Humpty Dumpty said . . . 'it means just what I choose it to mean—neither more nor less.' "

11-12; 131a-132a). The term "ingredients," however, does not even appear in the Aetna Underlying Policy and its appearance here represents a judicial creation from whole cloth. Yet "[i]t is fundamental that a court, in the guise of construing agreements, may not arrogate to itself the power of rewriting them." *Shamrock Casualty Company* v. *Mack*, 61 Misc. 2d 240, 243, 305 N.Y.S.2d 525, 529 (Sup. Ct. 1969). Thus, *Restatement (Second) of Contracts* §227, comment *c* at 508 (Tent. Drafts Nos. 1-7, 1973) states:

> The objective of interpretation in the general law of contracts is to carry out the understanding of the parties rather than to impose obligations on them contrary to their understanding: "the courts do not make a contract for the parties."*

The one case which has expressly relied upon transfers to third parties as the basis for determining the number of occurrences—*Morris Pincoffs Co.* v. *St. Paul Fire & Marine Ins. Co.*, 447 F.2d 204 (5th Cir. 1971)—did not involve an insurance policy with a batch clause. And the holding there would require a finding that there had been *one* occurrence here. The *Pincoffs* case arose from damage

*The District Court's conclusion that the parties to the Aetna Underlying Policy would never have thought to include the term "ingredients," "since an 'accident' could occur for purposes of the policy only after the ingredients were made into final goods and products which had been transferred to third persons," Opinion at 12, reveals the extent to which the Court's need to interject the notion of "ingredients" derives from its erroneous construction of "accident." Even accepting the District Court's premises, its statement is clearly wrong as a factual matter. If the Vitamin D3 resin "ingredients" had simply been sold to a third party as two lots at Harrison, that person's spraying them on corn cobs and then making and selling it as chicken feed to numerous chicken farmers would have yielded the same kind of damage as here. In short, even under the District Court's own logic there was no need for Diamond to have made the "ingredients" into final goods for an accident—as the District Court chose to define that term—to have taken place.

caused by contaminated bird seed sold by an importer to dealers who, in turn, resold to pet stores, which sold to bird owners, who ultimately fed the seed to their birds. There the court found eight separate occurrences in the sale of some 1000 bags of bird seed by the importer to eight different feed and grain dealers in Texas and Oklahoma over approximately one week. Thus, 1000 bags were divided among eight separate purchasers over a given period; and under the court's reasoning, each dealer's purchase of its aliquot number of bags constituted one occurrence. Applying this logic to the present case would result not in four occurrences based upon the four lots sold to Central Soya but rather one occurrence, because *Pincoffs* treated the purchase of a group of bags by each separate dealer, over the given period, as a single occurrence. *See also, Champion International Corporation* v. *Continental Casualty Company*, Ins. L. Rep. (Fire & Casualty Cas.) at 75-823 (S.D.N.Y., May 1, 1975).

A correct application of the rule that an insurance contract should be construed according to the expectations of the business which purchased the contract results in the batch clause reducing the number of occurrences to two. First, the damage involved in this case clearly "arose" out of the two Harrison lots as the word "arise" is commonly understood. Thus, *Webster's Third International Dictionary* at 117 (1961) defines "arise" in pertinent part (No. 4):

> a: to originate from a specified source . . . b: to come into being . . .

In short, the damage to the chickens originated from the defective Harrison lots and thus they are two lots of goods or products out of which damage arose. *Cf. George* v. *Douglas Aircraft Co.*, 332 F.2d 73 (2d Cir. 1964), *cert. denied*, 379 U.S. 904 (1964); *C.O. Falter, Inc.* v. *Crum & Forster Insurance Companies*, 79 Misc. 2d 981, 361 N.Y.S.2d 968 (Sup.

Ct. 1974); *Westchester Fire Insurance Co.* v. *Continental Insurance Co.*, 126 N.J. Super. 29, 312 A.2d 664 (1973), *aff'd*, 65 N.J. 152, 319, A.2d 732 (1974).

Second, the common understanding of the word "prepared" which modifies lot of "goods or products" makes clear that the expression applies to the Harrison lots.* Thus, *Webster's Third International Dictionary* at 1790-1791 (1961) defines the verb "prepare", in relevant part as:

> [No. 1a:] to make ready beforehand for some purpose; put into condition for a particular use, application or disposition . . .
> [No. 4a:] to put together; COMPOUND . . . prepared a vaccine from live virus . . . *prepared* the doctor's prescription . . . [No. 46:] MAKE, PRODUCE

and defines the adjective "prepared" at 1791 as:

> [No. 1:] made ready, fit, or suitable beforehand: READY, EQUIPPED
>
> [No. 2:] subjected to a special process or treatment . . .

Additionally, *The Random House Dictionary of the English Language* at 1137 (unabr. ed. 1966) gives the following definitions:

> PREPARE: . . . 1. to put in proper condition or readiness: to prepare a patient for surgery. 2. to get (a meal) ready for eating, as by proper assembling, cooking, etc. 3. to manufacture, compound or compose; to prepare a cough syrup . . .
>
> PREPARED: . . . 1. properly equipped; ready; prepared for a hurricane. 2. (of food) processed by the manufacturer or seller as by cooking, cleaning, or the like so as to be ready to serve or use with little or no further preparation . . .

*See *Random House Dictionary*, *infra*, which defines "lot" at 848 as "one of a set . . ." (No. 1). As discussed *infra*, insurance industry custom and usage applies this term to the earliest set of goods having a separate integrity and identity.

These dictionary definitions thus leave no doubt that the lot of goods or products encompassed by the batch clause were those two lots "compounded," "assembled," "composed," and "processed"—in short "prepared" at Harrison. Thus, the Harrison lots were "prepared" goods ready for use with only a small additional undertaking, just as prepared food in a delicatessen is ready for consumption after spreading on bread. *See, L. & S. Delicatessen, Inc.* v. *Carawana,* 143 N.Y.S.2d 350 (Sup. Ct. 1955); *People* v. *Wolen,* 161 Misc. 286, 291 N.Y.S. 665 (Magis. Ct. 1936).*

That "prepared" must refer to the two Harrison lots is further confirmed by the batch clause's reference to products "prepared or acquired". If Diamond's Louisville plant had acquired each of the two defective Harrison lots from another producer and had proceeded to do exactly what it actually did in converting those two lots into four lots of dry Vitamin D3 concentrate ("Nopdex"), there clearly would have been only two occurrences—regardless of the additional numbers of lots or batches of Nopdex "200" prepared and sold to Central Soya. Yet to rely upon the number of lots sold to Central Soya when the lots were originally prepared by Diamond, rather than acquired by it, would interject a purely artificial distinction into the construction of the batch clause and make the number of lots depend upon the irrelevant point of whether the "goods or products" were prepared or were acquired by the insured.

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*Thus, in *Thomas* v. *Winchester,* 6 N.Y. [2 Seld.] 397, 411 (1852), while imposing liability upon a chemist who had sold belladonna labeled as "dandelion" in a bottle which indicated that he had prepared the substance, the New York Court of Appeals obesrved:

> The word 'prepared' on the label, must be understood to mean that the article was manufactured by him or that it had passed through some process, under his personal knowledge of its true name and quality.

The plain meaning of the batch clause thus requires the result that there were two occurrences in this case—a result clearly reasonable and one intended by the inclusion of the clause. It is, of course, hornbook law that the object of interpretation is to give effect to the intention of the parties. "The cardinal rule, to which all other rules are subordinate, is that a contract is to be given that interpretation which will carry out the intention of the parties." 6 L. Simpson and R. Duesenberg, *Encyclopedia of New York Law: Contracts* §805 at 467 (1963). See also 1 Couch *Insurance* 2d §15:9 at 649-652 (1959):

> The object of the interpretation or construction of an insurance policy is to determine the intent of the parties, or their mutual understanding as expressed in writing, so that it may be given effect according to their real purpose and intention.

Furthermore, if the parties to an agreement have reduced their contract to writing but that writing is ambiguous, parole evidence is admissible to resolve ambiguities and apply the writing to its subject matter. *Conroff v. Occidental Life Insurance Co.*, 4 N.Y.2d 630, 152 N.E.2d 85, 176 N.Y.S.2d 660 (1958); L. Simpson and R. Duesenberg, *supra*, §808; *Restatement (Second) of Contracts* §240 (Tent. Drafts Nos. 1-7, 1973). Thus, should ambiguity be found in the construction of the batch clause, parole evidence would be admissible to resolve any such ambiguity.

The context in which an ambiguity might be said to arise in the present case is slightly different from the standard situation involving a dispute between two parties to a writing. The batch clause as well as the definition of occurrence both appear in the Aetna Underlying Policy, a contract between Diamond and Aetna, yet these two expressions in that contract are adopted in the Home Excess Policy, a contract between Diamond and Home. Put another way,

Home chose for itself and for Diamond the batch clause, as well as the definition of occurrence, as they appear in Aetna's contract with Diamond. Since Home chose these words as they appeared in the context of a pre-existing contract, surely the context in which these words appeared must be understood for the words themselves to be given meaning. Thus, *Restatement (First) of Contracts* §235(c) (1932) states at 319:

> A writing is interpreted as a whole and all writings forming part of the same transaction are interpreted together.*

Diamond, as well as Aetna, offered competent parole evidence to interpret the context in which the adopted definitions appear. Unfortunately, the District Court dismissed the proffered averments as "conclusory" statements of intent. Far from being conclusory, the Greening and Kaufmann affidavits discuss the negotiations between Diamond and Aetna which resulted in retention of the batch clause. These affidavits make clear that both parties knew Diamond wished to retain the batch clause in order to assure an interpretation that would reduce the number of occurrences under its retrospectively rated policy and to eliminate any possible ambiguity in that regard which might result from reliance simply upon the definition of occurrence. Thus, the affidavits submitted contained competent evidence as to intent. *See* 9 Wigmore *Evidence* §2472 (3d ed. 1940) which states at 233:

> . . . declarations of intention, though ordinarily excluded from consideration, are receivable to assist

*Comment *d* on Clause (c) at 322 states:

> Where a writing contains a sentence or paragraph of doubtful meaning when taken by itself, it may be made clear by other parts of the writing, and even words which have in themselves a clear meaning may be controlled and given a different meaning because of other parts of the writing.

> in *interpreting an equivocation*,—that is, a term which, upon application to external objects, is found to fit *two or more of them equally*.

Cf. Rule 701 of the Federal Rules of Evidence.

Thus, competent parole evidence explains the intent of Diamond and Aetna with respect to the words in question, an intent which Home clearly adopted when it chose the words manifesting that intent. This obviates the District Court's argument that parole evidence should not be considered, since Diamond and Aetna's intent was not communicated to Home. One additional factor renders the District Court's position untenable. The *Restatement (Second) of Contracts* §227 (Tent. Drafts Nos. 1-7 1973) provides at 507:

> (2) Where the parties have attached different meanings to a promise or agreement or a term thereof, it is interpreted in accordance with the meaning attached by one of them if at the time the agreement was made
>
> (a) that party did not know of any different meaning attached by the other, and the other knew the meaning attached by the first party; or
>
> (b) that party had no reason to know of any different meaning attached by the other, and the other had reason to know the meaning attached by the first party.

Subsection (b) would most clearly apply to the present case. Certainly Home has adduced no evidence which even suggests that Diamond had reason to know of the construction which Home now attempts to foist upon the batch clause. On the other hand, the Burns Affidavit in support of Home's motion for summary judgment, indicates that Home knew of the $100,000 per occurrence deductible (13a), while the subsequent Mella Affidavit in opposition to Dia-

mond's cross motion states only that Home "was not advised" of the $100,000 per occurrence deductible (62a).* This deductible, however, should have clearly put Home on notice as to Diamond's intent with regard to the lot clause. Even if this were not the case, Home's carelessness in adopting a provision by reference should, as a matter of law, provide a basis for holding that Home had reason to know Diamond's intent because normal business practice would have put Home on notice.

C. The District Court erred in not applying the rule of *contra proferentem* to resolve any ambiguity concerning the number of occurrences in Diamond's favor.

Even if this Court should conclude that the insurance language in question makes Home's position on the number of occurrences as reasonable as Diamond's, this ambiguity should be resolved against Home, the insurer, and in favor of Diamond, the insured. This result is dictated by New York's rule that any ambiguity in an insurance policy is construed against the insurer and in favor of the insured, a rule that is summarized in the Latin maxim *contra proferentem*. *Pan American World Air, Inc.* v. *Aetna Casualty and Surety Co.*, 505 F.2d 989 (2d Cir. 1974); *Champion International Corporation* v. *Continental Casualty Company*, Ins. L. Rep. (Fire & Casualty Cas.) at 75-823 (S.D.N.Y., May 7, 1975); *McGroarty* v. *Great American Insurance*, 36 N.Y.2d 358, 329 N.E.2d 172, 368 N.Y.S.2d 485 (1975); *Sincoff* v. *Liberty Mutual Fire Insurance Co.*, 11 N.Y.2d 386, 183 N.E.2d 899, 230 N.Y.S.2d 13 (1962); *State Farm Mutual Automobile Insurance Co.* v. *Bush*, 46 App. Div.2d 958, 362 N.Y.S.2d 220 (1974). Indeed, New York

*Incredibly, the Mella Affidavit apparently asked the District Court to believe that Home would have *and did* incorporate expressions from the Aetna Underlying Policy by reference without having seen the policy.

applies this rule quite stringently by requiring the insurer to demonstrate that his position is the only *reasonable construction;* conversely, if the insured submits "a possible construction of the provision—even though not the only construction—it must be accepted since the ambiguity will be construed against the insurance company." *Thomas* v. *Mutual Benefit Health & Accident Ass'n,* 123 F. Supp. 167, 170 (S.D.N.Y. 1954), *aff'd,* 220 F.2d 17 (2d Cir. 1955). *See also Pan American World Air, Inc.* v. *Aetna Casualty & Surety Co., supra; Datalab, Inc.* v. *St. Paul Fire & Marine Insurance Co.,* 347 F. Supp. 36 (S.D.N.Y. 1972); *Sinoff* v. *Liberty Mutual Fire Insurance Co., supra.*

This case presents a clear instance of a dispute between insurer and insured over the contract of insurance. The Home Excess Policy adopts by reference the definition of occurrence and the batch clause in the Aetna Underlying Policy. As an insurance company and author of the excess policy with Diamond, Home was obviously in a superior position to protect itself against any possible ambiguities arising out of the language that it chose to adopt. Thus, any ambiguity with respect to the number of occurrences should clearly be resolved against Home which wrote the Home Excess Policy in issue here.

The application of *contra proferentem* to the dispute between Home and Aetna cannot be resisted on the grounds that the present controversy is a "dispute between insurers." Indeed, Diamond has an obvious financial interest in whether there were four occurrences or two. If there were four occurrences, Diamond would be forced to absorb up to $400,000 of the total damage because of the $100,000 deductible per occurrence. On the other hand, if there were two occurrences, Diamond would be compelled to absorb only up to $200,000 of the total damage. Thus, Diamond has a very real financial interest in a determination that there were two occurrences.

Such an analysis led this Court to apply the New York rule of *contra proferentem* in the *Pan American* case, over objections that only a conflict between insurers was involved. Briefly summarized, that case was a suit by Pan American against its all risk insurers and both its private and government war risks insurers with respect to the extent of insurance coverage for the destruction of a Pan American jet hijacked and destroyed by Palestinian terrorists. The all risk insurers' standard policies contained certain exclusions as to war damage which exclusions constituted the language of coverage in the private war risk policies. In holding that the case was not simply a dispute between insurers over whose policy covered the loss, this Court pointed out that the insured had a clear financial stake in coverage by the all risk insurers, because if these were found not liable on the basis of certain war damage exclusions, Pan American would suffer a $288,000 gap in coverage. In this case, Diamond will suffer a gap in coverage of up to $200,000 if Home's construction of the batch clause is accepted. Thus, this Court's opinion in *Pan American*, which rejects the notion that *contra proferentem* is inapplicable merely because there may be at least two insurers involved in the controversy and one insurer may be found agreeing with the insured, applies with equal force to the present case:

> The all risk insurers claim that *contra proferentem* is not applied where the dispute is in reality between groups of insurers. While their statement of principle may accurately represent the law in some jurisdictions, see, e.g., *Boston Insurance Co.* v. *Fawcett*, 357 Mass. 535, 538, 258 N.E.2d 771, 776 (1970), it does not state New York law. 505 F.2d at 1002.

London Assurance Corp. v. *Thompson*, 170 N.Y. 94, 62 N.E. 1066 (1902). *See*, e.g., *Float-Away Door Co.* v. *Continental Casualty Co.*, 372 F.2d 701 (5th Cir. 1966), *cert. denied*, 389

U.S. 823 (1967); *Broome County Co-operative Fire Insurance Co.* v. *Aetna Life and Casualty Co.*, 75 Misc.2d 587, N.Y.S.2d 778 (Sup. Ct. 1973); *Jamestown Mutual Insurance Co.* v. *Nationwide Mutual Insurance Co.*, 266 N.C. 430, 146 S.E.2d 410 (1966).

The recent case of *Champion International Corp.* v. *Continental Casualty Co.*, Ins. L. Rep. (Fire & Casualty Cas.) at 75-823 (S.D.N.Y., May 1, 1975) in effect applies this Court's reasoning on the applicability of *contra proferentem* to a set of facts strikingly similar to those in the instant case In *Champion*, the insured plaintiff bought a large number of vinyl plywood panels from another company and re-sold them to other manufacturers for installation in houseboats, campers, etc. Many of these panels were defective and resulted in substantial damages, though no damage sustained by any single vehicle was greater than $5,000. Champion was insured by Liberty Mutual as primary carrier under a comprehensive general liability policy, providing a limit of $100,000 per occurrence subject to a $5,000 per occurrence deductible, with occurrence defined as here. Additionally, Champion had an excess policy from Continental that contained a definition of occurrence equivalent to Liberty's policy and a provision effectively adopting Liberty's "terms and conditions" by reference. While Liberty had apparently accepted Champion's position that liability arose from one occurrence, Continental maintained that there had been one occurrence for each vehicle sustaining damage. The District Court resolved the ambiguity over the number of occurrences against Continental, the excess insurer:

> . . . I find in favor of the [insured] because I find that the contested language is ambiguous. The interpretation urged by the [insured] may not be the only reasonable interpretation, but it is a reasonable one. That is all the [insured] is required to prove. *Champion, supra*, at 825.

D. The District Court erred in not holding that Diamond's competent evidence on industry custom and usage required a finding of two occurrences.

Pertinent industry custom and usage constitutes an important aid in the construction of insurance policies.

> Evidence of usage is . . . admissible to apply a written contract to the subject matter of the action, to explain expressions used in a particular sense by particular persons as to particular subjects, to give effect to language in a contract as it was understood by those who made it. *Smith* v. *Clews*, 114 N.Y. 190, 193, 21 N.E. 160, 161 (1889)

See 1 Couch *Insurance* 2d § 15:59 (1959). Furthermore, the existence of an ambiguity is not a necessary predicate to the admissibility of evidence as to custom or usage. Thus, *Restatement of the Law of Contracts Second* §246, comment *d* (Tent. Draft Nos. 1-7, 1973) states at 564:

> Language and conduct are in general given meaning by usage rather than by the law, and ambiguity and contradiction likewise depend upon usage. Hence usage relevant to interpretation is treated as part of the context of an agreement in determining whether there is ambiguity or contradiction as well as in resolving ambiguity or contradiction. There is no requirement that an ambiguity be shown before usage can be shown . . .

Finally, knowledge of pertinent custom or usage may be presumed. Hence, in *Gelb* v. *Automobile Insurance of Hartford*, 168 F.2d 774 (2d Cir. 1948), a yacht owner was presumed to have known the meaning that custom and usage ascribed to the term "lay-up" used in his yacht insurance policy. In reaching that conclusion this Court stated:

> . . . evidence to interpret the meaning of a term used in a contract is undobutedly competent. Parties are

> presumed to contract with reference to general customs and usages which explain the specific meaning of a term used and personal knowledge of the customary meaning need not be had by the parties to the contract. 168 F.2d at 775.

Diamond has offered in the Collins Affidavit (37a-39a) uncontradicted* evidence on insurance industry custom governing the batch clause. Based upon his eight years in the adjustment, examination and supervision of claims for the Insurance Company of North America, his handling of a number of claims to which the batch clause applied, and his participation in interpreting the batch clause with respect to many products liability claims, Mr. Collins, now an Assistant Vice President for the insurance brokerage firm of Alexander & Alexander where he had been employed as casualty claims director for three years, averred that

> The customary understanding and usage in the industry is that once a batch or lot has separate integrity and an administrative number for accounting and production purposes, there is a lot within the meaning of the batch clause. The number of batches or lots that is relevant in determining the number of "occurrences" is the number identifiable at the stage where the "accident" occurred. The first stage when (a) the product is divided into identifiable batches *and* (b) an accident occurs or has occurred is the stage relevant to application of the batch clause. Collins Affidavit at ¶4 (38a).

The District Court rejected this evidence because: (1) sufficient facts were not shown to demonstrate the qualifications of the witness to testify on insurance industry custom

*The Mella Affidavit in no way contradicts Diamond's submission as to a custom and usage since Home's affiant states only that he was not aware of such custom and adds in a parenthetical that 'Even if there were an industry-wide understanding . . . which there is not . . .," (61a). This redundant denial of a subjunctive hardly represents testimony to contradict the Collins Affidavit.

and usage and (2) the proffered averments were conclusory statements as to general understanding not supported by evidentiary facts. As to the first contention, the affidavit's recitation of Mr. Collins' background and experience surely belies the District Court's position on qualification. Thus, *Miele* v. *Rosenblatt*, 164 App. Div. 604, 150 N.Y.S.323, *aff'd*, 221 N.Y. 567, 116 N.E. 1062 (1917) allowed a button cutter with several years experience in his field to describe what kind of tongs were customarily used in his field and allowed another similarly experienced cutter to testify as to the method and tools customarily used to sharpen drills.* To the extent that the District Court's conclusion rests upon the assumption that one witness alone cannot establish the existence of custom, it is, of course, wholly incorrect. 7 Wigmore *Evidence* §2053 (3d ed. 1940).

As to the District Court's second premise, that, too, is incorrect. Thus, 7 Wigmore *Evidence* §1954 at 84 (3d ed. 1940), rejects this notion as unsound:

> It has sometimes been said that a witness to trade usage may state only specific instances, or must at least mention one or more in support of his statement of the general practice. This notion is traceable to some remarks of Lord Mansfield and later judges, which do not justify it. There have indeed been judges who have refused, on all the facts of a case, to credit witnesses to usage, who could not adduce instances in verification. But there is no rule of exclusion. The usage is itself a fact, and the Opinion rule does not treat such testimony as an inference from data which can be adequately stated without the inference.

Cf. Rules 702-705 of the Federal Rules of Evidence.

Neither *Appelgate* v. *Top Associates, Inc.*, 425 F.2d 92 (2d Cir. 1970) nor *Union Insurance Society of Canton, Ltd.*

*Hence a Federal District Court in a diversity action has excluded evidence from an affiant whom governing State law would find competent to testify. *See,* Rule 601 of the Federal Rules of Evidence.

v. *William Gluckin & Co.*, 353 F.2d 946 (2d Cir. 1965), supports the District Court's rejection of the Collins Affidavit, since neither case deals with competence to testify about custom and usage.

E. The District Court erred in not denying all motions for summary judgment because there existed genuine issues of material fact

This brief has already set forth Diamond's contention that the plain meaning of "occurrence" and the batch clause required the District Court to grant Diamond's motion for summary judgment and deny Home's. If those terms are ambiguous and the rule of *contra proferentem* does not apply to this case, then the District Court should have denied all motions for summary judgment because there existed genuine issues of material fact as to: (1) Diamond and Aetna's intent in adopting the batch clause and (2) the existence of insurance industry custom and usage concerning the batch clause.* These factual issues made summary judgment impossible. *See, e.g., Hartford Accident & Indemnity Co.* v. *Wesolowski*, 33 N.Y.2d 169, 305 N.E.2d 907, 350 N.Y.S.2d 895 (1973); 6 L. Simpson and R. Duesenberg, *Encyclopedia of New York Law: Contracts* § 802 (1963).

The District Court's out-of-hand rejection of the affidavits of Aetna and Diamond for technical deficiencies violates the cardinal rule that affidavits of those opposing summary judgment are to be liberally treated. Thus, 10 C. Wright and A. Miller *Federal Practice and Procedure* § 2738 at 708-9 (1973) states:

> The cases seem to indicate that judges will be quite demanding in their examination of the moving

*This alternative argument assumes that the District Court should have properly found that Home's affidavits, especially the Mella Affidavit, in fact, contradicted the averments made by Diamond's and Aetna's affiants, a point which is conceded only for the sake of this argument.

> parties' papers, but will treat the papers of the party opposing the motion indulgently. This practice has two aspects. First, because the burden of proving that there is no genuine issue of material fact rests on the moving party, the opposing party is entitled to all of the favorable inferences that reasonably may be drawn from the papers before the court. Second, the courts strictly scrutinize the papers of the moving party to assure compliance with the requirements of Rule 56(e). . ."

See also, 6 J. Moore *Federal Practice* ¶56.15[3] at 2337-2338 (2d ed. 1974). Indeed, in reviewing the *grant* of summary judgment, an appellate court must take all factual inferences in favor of the party against whom summary judgment was granted. 10 C. Wright and A. Miller, *supra*, § 2727.

CONCLUSION

The District Court erred in holding that the plain meaning of the batch clause as well as the definition of occurrence in Diamond's insurance policy results in four, rather than two, occurrences in this case. In so doing, the District Court overlooked the common meaning of the words employed in these provisions and the nature of the risks for which Diamond had sought insurance. Additionally, the court below failed to apply the rule of *contra proferentem* to resolve against Home and in favor of Diamond any ambiguity in the policy as to determination of the number of occurrences. Furthermore, the District Court improperly disregarded the competent and uncontroverted evidence of Diamond and Aetna as to intent and as to insurance industry custom with respect to the batch clause.

For all of the foregoing reasons the decision of the District Court should be reversed, the judgment vacated, and the case remanded with a direction either (i) to enter an order granting Diamond's motion for summary judg-

ment or, in the alternative, (ii) to enter an order denying all motions for summary judgment and to conduct such further proceedings as may be appropriate.

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Respectfully submitted,

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